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IDENTIFYING AND REDUCING THE CROSS-BORDER FINANCIAL CRIME RISKS INHERENT IN THE AFRICAN CONTINENTAL FREE TRADE AREA

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ABSTRACT

On March 21, 2018, at the 10th Extraordinary Summit of the African Union, Close to Fifty (50) African Union Member States signed the African Continental Free Trade Area (AfCFTA) agreement, thereby creating the largest free trade area in the world. The agreement officially entered into force on May 30, 2019, after ratification of the agreement by 22 countries. As of 31 May 2022, only 43 of the 54 African countries that signed the Agreement Establishing the AfCFTA in March 2018, had deposited Instruments of Ratification with the Chairperson of the African Union Commission.

But while the AfCFTA is seen as a means of promoting economic growth and investment between African states, it also has a darker side. Like the Free Trade Zones in Morocco, Gambia, Djibouti and Nigeria, it carries the potential exposures to illicit trade and financial crime, including but not limited to illicit finance activity, drug trafficking and trade-based money laundering.

This research provides Authorities managing Free Trade Zones, Business Enterprises, Financial Institutions and Dedicated Free Zone Customs, Police and Immigration Command assigned to deal with aspects of movement of goods and persons in and out of the Free Zones with a clear understanding of the cross-border financial crime risks associated with the African Continental Free Trade Area and the risk control measures that combines human intelligence with artificial intelligence, machine learning technology and robotic process automation to combat cross-border financial crimes in the African Continental Free Trade Area.

This research paper advocates for public-private partnerships through the collective action theory. A partnership between Authorities managing Free Trade Zones, Business Enterprises, Financial Institutions and Dedicated Free Zone Customs, Police and Immigration Command assigned to deal with aspects of movement of goods and persons in and out of the Free Zones for information sharing can help identify and report potential financial crimes.

While many Authors have written research papers on intra-African trade, none of those research papers explained how countries can assess and mitigate financial crime risks in free trade zones. This research paper describes the ways in which cross-border financial crime risks can be assessed and adequately addressed by the authorities managing Free Trade Zones. This research paper analyses the risk assessment topic in line with the African Continental Free Trade Area with a focus on Free Trade Zones in Nigeria.

This research paper would help authorities managing Free Trade Zones, commercial organisations and business enterprises to identify, prevent and mitigate cross-border financial crime risks. Zone managements and Business enterprises that implement the risk-based

approach, in line with the guidance given in this research paper, will be well-placed to avoid the consequences of inappropriate de-risking behaviour.

Index Terms - The African Continental Free Trade Area, Free Trade Zones, Illicit Finance Activity, Drug Trafficking, Trade Based Money Laundering, Artificial Intelligence

1. INTRODUCTION

On March 21, 2018, at the 10th Extraordinary Summit of the African Union, Close to Fifty (50) African Union Member States signed the African Continental Free Trade Area (AfCFTA) agreement, thereby creating the largest free trade area in the world.¹

The agreement officially entered into force on May 30, 2019, after ratification of the agreement by 22 countries.² As of 31 May 2022, only 43 of the 54 African countries that signed the Agreement Establishing the AfCFTA in March 2018, had deposited Instruments of Ratification with the Chairperson of the African Union Commission.³ Nigeria deposited its Instrument of Ratification of the AfCFTA agreement on 5 December, 2020, becoming the 34th member state to formally ratify the treaty. The deposit came an hour before the opening of a summit of African heads of state where they proclaimed the Johannesburg Declaration formally fixing trading to start on 1 January 2021 as earlier scheduled.⁴

The AfCFTA will cover a market of 1.2 billion people and a gross domestic product (GDP) of \$2.5 trillion, across all 55 member States of the African Union. In terms of numbers of participating countries, AfCFTA will be the world's largest free trade area since the formation of the World Trade Organization.⁵

The general objectives of the African Continental Free Trade Area are to:

- (a) Create a single market for goods, services, facilitated by movement of persons in order to deepen the economic integration of the African continent and in accordance with the Pan African Vision of “An integrated, prosperous and peaceful Africa” enshrined in Agenda 2063;
- (b) Create a liberalized market for goods and services through successive rounds of negotiations;

- (c) Contribute to the movement of capital and natural persons and facilitate investments building on the initiatives and developments in the State Parties and Regional Economic Communities (RECs);
- (d) Lay the foundation for the establishment of a Continental Customs Union at a later stage;
- (e) Promote and attain sustainable and inclusive socio-economic development, gender equality and structural transformation of the State Parties;
- (f) Enhance the competitiveness of the economies of State Parties within the continent and the global market;
- (g) Promote industrial development through diversification and regional value chain development, agricultural development and food security; and
- (h) Resolve the challenges of multiple and overlapping memberships and expedite the regional and continental integration processes.⁶

For purposes of fulfilling and realizing the objectives set out above, State Parties shall progressively eliminate tariffs and non-tariff barriers to trade in goods⁷ and progressively liberalize trade in services.⁸

State Parties must also cooperate on investment, intellectual property rights and competition policy; ⁹ cooperate on all trade-related areas;¹⁰ and cooperate on customs matters and the implementation of trade facilitation measures.¹¹

State Parties shall establish a mechanism for the settlement of disputes concerning their rights and obligations; ¹² and establish and maintain an institutional framework for the implementation and administration of the African Continental Free Trade Area.¹³

The Agreement establishing the African Continental Free Trade Area covers trade in goods, trade in services, investment, intellectual property rights and competition policy.¹⁴ The Protocols on Trade in Goods, Trade in Services, Investment, Intellectual Property Rights, Competition Policy, Rules and Procedures on the Settlement of Disputes and their associated Annexes and Appendices form part of the Agreement establishing the African Continental Free Trade Area, subject to entry into force.

1.1. Statement of the Problem

But while the AfCFTA is seen as a means of promoting economic growth and investment between African states, it also has a darker side. Like the Free Trade Zones in Morocco, Gambia, Djibouti and Nigeria, it carries the potential exposures to illicit trade and financial crime, including but not limited to illicit finance activity, drug trafficking and trade-based money laundering.

A clear challenge of Free Trade Zones is the unique balance of promoting a business friendly, open environment while still implementing anti-money laundering and counter terrorist financing measures in Free Trade Zones in Nigeria.

1.2. Research Questions

This research intends to explore the following questions:

I. What are the cross-border financial crime risks in Free Trade Zones? II. How can countries assess the cross-border financial crime risks and vulnerabilities in the Free Trade Zones, business and supply chains? III. What measures can be adopted by countries to remediate or mitigate the cross-border financial crime risks in Free Trade Zones?

1.3. Objectives of the Study

The focus of this research study is on providing Authorities managing Free Trade Zones, Business Enterprises, Financial Institutions and Dedicated Free Zone Customs, Police and Immigration Command assigned to deal with aspects of movement of goods and persons in and out of the Free Zones with a clear understanding of the cross-border financial crime risks associated with the African Continental Free Trade Area and the risk control measures that combines human intelligence with artificial intelligence, machine learning technology and robotic process automation to combat cross-border financial crime in the African Continental Free Trade Area. The analytical approach adopted by this research paper ensures that readers will achieve the following:

- i. Identify cross-border financial crime risks in Free Trade Zones.
- ii. Assess where the cross-border financial crime risks and vulnerabilities are in the Free Trade Zones, business and supply chains.
- iii. Determine how cross-border financial crime risks in Free Trade Zones can best be remediated or mitigated through policy, training and collaboration.

1.4. Significance of the Study

This paper is structured to help countries and reporting entities better understand what the risk-based approach is and take inventory of their financial crime risks relating to Licensing, Monitoring and Regulation of Free Zones; Management of Free Zones; Incentives and Concessions; Banking Business; Movement of Persons, Goods, etc in and out of Free Zones; Abandoned Goods; Manufacturing and Processing; Registration of Vehicles; Issue of Driving Licences; Customs, Police and Immigration; and Customs Procedures; Free Zone Tariffs and Charges; and Provision of Services outside the Free Zones. It will also help in implementing effective mitigation measures and in monitoring the financial crime risks Nigeria Export Processing Zones Authority (hereinafter referred to as the Authority)/Zone Management may have or encounter as part of their activities and business relationships.

1.5 Scope and Limitation of the Research

This research study identifies the cross-border financial crime risks that are of priority concern to African Continental Free Trade Areas and shows how countries can assess and mitigate these risks. The purpose of the analysis is to help the public and private sectors recognize and understand the importance of assessing and mitigating the financial crime risks at a zonal level.

The remaining part of the research study is organized as follows: Section 2 provides an overview of the conceptual framework of this research. Section 3 outlines the theoretical framework of this research. Section 4 summarizes the research methodology; Section 5 provides the literature review; Section 6 identifies the cross-border financial crime risks that are of priority concern to African Continental Free Trade Areas and demonstrates how countries can assess these risks. The purpose of the analysis is to help the public and private sectors recognize and understand the importance of assessing risk at a zonal level; Section 7 describes the ways in which financial crimes can be adequately addressed in Free Trade Zones; Section 8 provides concluding remarks on the research problem and solutions while Section 9 lists the books, scholarly articles, websites, and other sources used for this research topic.

2. CONCEPTUAL REVIEW

This section provides an overview of the conceptual framework of this research.

2.1 Free Trade Zones

The African Continental Free Trade Area presents countries in Africa with an exceptional lifeline to enhance the competitiveness of the economies of State Parties within the continent and the global market¹⁵ and promote industrial development through diversification and regional value chain development, agricultural development and food security.¹⁶

Business enterprises in countries across Africa can take advantage of the lofty opportunities provided by the agreement to seamlessly trade among themselves in specially designated trade-promotion areas also referred to as Free Trade Zones.

'Free Trade Zone' refers to an area designated by a country or jurisdiction, where goods that enter this area are not subject, or are subject to lower import or export duties than those that would apply if such goods were declared for release for free circulation, at the moment when they enter it. Facilities used for temporary storage or for the customs warehousing procedure are not deemed to be Free Trade Zones.¹⁷ Free Trade Zones are created within jurisdictions to promote trade, support new business formation, and encourage foreign direct investment. They provide a preferential environment for goods and services primarily associated with exports, whereby a minimum level of regulation is imposed on those companies approved to operate within the zone. Additional benefits include exemptions from duty and taxes, simplified administrative procedures and duty free imports of raw materials, machinery, parts and equipment.¹⁸

There are as many names for these specially designated trade-promotion areas as there are countries that conduct international trade. In addition to free trade zone, some of the other common terms for these areas include special economic zones, foreign trade zones, and export processing zones.¹⁹ The International Convention on the Simplification and Harmonization of Customs Procedures (Revised Kyoto Convention) uses the term "free zones," which the revised convention describes as "a part of the territory of a Contracting Party where any goods introduced are generally regarded, insofar as import duties and taxes are concerned, as being outside the Customs territory." Part 11 of the Investment Procedures, Regulations and Operational Guidelines for Free Zones in Nigeria, 2004 also uses the term "free zones," to mean Export Processing Zones, Border Free Zones, Free Trade Zones, Export Processing Factories and Export Processing Farms established pursuant to the Nigeria Export Processing Zones Act No 63 of 1992. Part 7 of the Investment Procedures, Regulations and Operational Guidelines for Free Zones in Nigeria, 2004 uses the term "Free Trade Zones," to mean export processing zones created under the Nigeria Free Trade Zones Act No. 63 of 1992.

Any business enterprise which proposes to undertake an approved activity in any of the 44 free trade zones in Nigeria,²⁰ shall apply to the Nigeria Export Processing Zones Authority (hereinafter referred to as the Authority) in writing for permission to do so and shall submit such documents and information in support of its application, as the Authority may require.²¹ The licensing, monitoring, and regulation of all free zones in Nigeria is vested in the Authority.²² Application to undertake an approved activity shall be considered within five working days of its acknowledgement and the applicant notified in writing of approval or otherwise.²³ Subject to the provisions of the Nigeria Export Processing Zones Act 1992, the Authority may grant, subject to such terms and conditions as it thinks fit, approval for an enterprise to undertake the approved activity specified in its application.²⁴ These activities could be: Manufacturing of goods for export; Warehousing freight forwarding and customs clearance; Handling of duty free goods (transshipment, sorting, marketing, packaging, etc.); Banking, stock exchange and other financial services; insurance and re

insurance; Import of goods for special services, exhibitions and publicity; International Commercial Arbitration Services; Activities relating to integrated zones; and Other activities deemed appropriate by Nigeria Export Processing Zones Authority.²⁵

Upon receipt of approval to undertake approved activity in a Zone, an applicant shall apply to the Authority/Zone Management for licensing as an approved enterprise as provided by the Act.²⁶ The Authority/Zone Management may grant approval for one or more of the following Licences:

A. Free Zone Developers License

License granted by the Authority to either a public, private entity or a combination of the two for the establishment, operation and management of a Free Zone in Nigeria under the supervision, monitoring and regulation by the Nigeria Export Processing Zones Authority.²⁷

B. Free Zone Enterprise License

License granted by the Authority/Zone Management for an enterprise to undertake an approved activity within a Free Zone. These activities could be:

- a. Manufacturing
- b. Trading
- c. Service Provision²⁸

C. Export Processing Factory/Export Processing Farm License

License granted by the Authority to an export oriented manufacturing enterprise of farm located in the customs territory which has the capacity to export over 75% of its production.²⁹

Upon a Licence being granted to an approved entity by the Authority/Zone Management, the Authority shall cause all relevant details concerning such enterprise to be entered in the FZ Register and for a Certificate of Registration, duly executed by or on behalf of the Authority/Zone Management, to be issued.³⁰ The Management of Federal Government Free Zones is vested in the Authority while those of States and private entities is vested in the licensees.³¹

The objects of each Free Zone Enterprise shall be to carry on all such business within the area of the Free Zone as the Authority may permit under the terms of the Licence issued in respect of the Free Zone Enterprise (as the same may be amended from time to time by the Authority) and elsewhere in accordance with all applicable laws and regulations, and all business and other matters ancillary, conducive or related thereto. Such matters will include power for each Free Zone Enterprise to borrow, grant security, guarantee any obligation of any person or indemnify

any person, to enter into all types of banking and financial transactions, to issue, make endorse or draw any negotiable instruments (such as cheques, bills of exchange, promissory notes or bills of lading) in relation to its business and power for each Free Zone Enterprise to make, alter or dispose of any investments (whether or not within Nigeria) in relation to its business.³²

No person can enter, remain in or reside in a Free Zone in Nigeria without the prior permission of the Authority. No retail trade can be conducted within the Free Zone without the prior approval of the Authority and which may be subject to such terms and conditions as may be imposed by the Authority. Access to the Zone is restricted and subject to the presentation of a pass and such conditions as the Authority may stipulate from time to time in writing.³³ These features and many more is what makes Free Trade Zones vulnerable to financial crimes.

In 2016, the Central Bank of Nigeria issued guidelines for banking operations in the free zones in Nigeria to regulate the activities of Banks in free zones and combat financial crimes in free zones in Nigeria. Regulation 8(a) of the Guidelines for Banking Operations in the Free Zones in Nigeria, 2016 prohibits the opening an account for a customer in contravention of the Know-Your Customer (KYC) principles while Regulation 9 mandates Banks within the free zones to ensure strict adherence to the provisions of the Money Laundering (Prevention and Prohibition) Act, 2022 and the Terrorism (Prevention and Prohibition) Act, 2022

2.2 The Risk-Based Approach

Risk can be defined as the likelihood of an event and its consequences.³⁴ In simple terms, risk can be seen as a combination of the chance that something may happen and the degree of damage or loss that may result from such an occurrence.³⁵ In the context of financial crimes, risk means:

- At the national level: threats and vulnerabilities presented by financial crimes that put at risk the integrity of a Country's financial system and the safety and security of its citizens.
- At the reporting entity level: threats and vulnerabilities that put the reporting entity at risk of being used to facilitate financial crime.³⁶

In the context of financial crime, a risk-based approach is a process that encompasses the following:

- The risk assessment of business activities and clients using certain prescribed elements;
- The mitigation of risk through the implementation of controls and measures tailored to the identified risks;
- Keeping client identification and, if required, beneficial ownership and business relationship information up to date in accordance with the assessed level of risk; and
- The ongoing monitoring of transactions and business relationships in accordance with the assessed level of risk.³⁷

The steps the Authority managing Free Trade Zones should take for the licensing, monitoring, regulation and management of Free Trade Zones depends on how it initially evaluates a business enterprise. The Management of Free Trade Zones must ask all but its lowest risk business enterprises to complete its 'Project Due Diligence' questionnaire – which helps establish a high or medium risk of them falling below the standards set by the Authority managing Free Trade Zones.

Risk profiling helps the Authority managing Free Trade Zones to focus its efforts where they are most needed. For example, business enterprises may present a higher risk of bribery, corruption and money laundering because of the nature of their business and where they are based. All medium risk business enterprises must get a review. High risk business enterprises must get a more detailed review to better understand the risk and put in steps to tackle it; this may mean visiting their principal place of business.

Financial Crime risks are affected by various factors, including the strength of policies, laws and institutions to protect against financial crime where the company operates. In areas of weaker governance, the Authority managing Free Trade Zones will find that the risk that the company may be involved in financial crime through its businesses is greater. Using desk-based research to elicit information about the company's anti-money laundering record, including public information in standard industry guides, periodicals, and major publications, the Authority managing Free Trade Zones will recognize the heightened risks of exposure to financial crime in some emerging economies as well as that financial crime may occur in developed markets. The Authority managing Free Trade Zones can then priorities those business enterprises identified as being exposed to the highest risks and ask them to complete a self-assessment questionnaire. The self-assessment questionnaire should be structured around the key areas of the company's risk profile and provide the Authority managing Free Trade Zones with information on the policies, procedures and practices the company has in place to effectively manage these risks.

Where the results of the self-assessment highlight minor areas for improvement, the Authority managing Free Trade Zones should work with the company to develop corrective actions and agree on a timescale for material progress towards compliance.

Where the results reveal more significant issues, an on-site audit should be conducted by the Management of Free Trade Zone's independent auditor. This includes criteria on the company's systems and controls – with a specific section focusing on the company's monitoring system's programming, methodology, and effectiveness.

In the event of serious and/or persistent non-compliance, or where the company fails to demonstrate a willingness to improve performance, the Authority managing Free Trade Zones reserves the right to terminate the business relationship.

3. THEORETICAL FRAMEWORK

In the area of combating financial crime, the topic of Collective Action has transitioned from being a major academic think-piece into a very concrete policy issue: Collective Action is now a kind of catch-all term for industry standards, multi-stakeholder initiatives, and public-private partnerships (PPPs). It may take on the form of an anti-corruption declaration, an Integrity Pact (or an “Island of Integrity”), a principle-based initiative or, even, a certifying effort.³⁸

The World Bank Institute (WBI), in its *Fighting Corruption Through Collective Action, A Guide for Business*, defines – and justifies – “Collective Action” as a collaborative and sustained process of cooperation between stakeholders. It increases the impact and credibility of individual action, brings vulnerable individual players into an alliance of like-minded organizations and levels the playing field between competitors. Collective action can complement or temporarily substitute for and strengthen weak local laws and anti-corruption practices.³⁹

The history of early experiments with Collective Action in relation to combating financial crime has come with success stories. Same can be said of the recent experiment with Collective Action.

Early success: Wolfsberg

During the 1990s, regulation of the financial industries dramatically increased, anti-money laundering standards abounding in particular. For banks, it seemed that regulators had gone out of control. It was as if they were continuously raising the bar for compliance without really understanding the challenges for business. And, though complaints about singling out by regulators were rife, competitors had not yet considered the possibility of sitting down together and drafting an anti-money laundering compact of their own. Indeed, when civil society organizations⁵⁰ and far-sighted bankers first raised the idea, most executives responded semi-automatically with concerns about breaching laws on anti-competitive trusts. Perhaps this was a self-protective reflex, aimed at preventing their institutions from rushing prematurely into an ill-considered adventure. The common efforts were, nonetheless, the starting point for an initiative that served as a pattern for Collective Action initiatives to come: the Wolfsberg Banking Group. Initially, Wolfsberg’s standards were relatively simple. They did not really go beyond what regulators had already decided. However, the activation of the private sector was a sensation in itself, drawing close to 200 journalists to a press conference. The fact that banks – so frequently criticized for laundering drug money and hiding dictator’s loot – would go on the offensive, was apparently spectacular in 2000. The group met intensively and produced further compacts. It rapidly established itself as a crucial industry reference group for regulators and international public bodies, not unlike the FATF. Now, beyond its internal meetings, the Wolfsberg Group even holds an annual “Wolfsberg Forum”, inviting all relevant regulators and competitors to participate and comment on its annual catalogue of working documents. Thus, with time, the Wolfsberg Group matured into a strong self-regulatory body of the financial sector, one capable of dealing with issues of money laundering, the financing of terrorism, corruption, and embargo-busting.⁴⁰

Success: Building Trust through Public-Private Dialogue on Anti-Corruption - UNGC Nigeria

This Collective Action project focuses on building alliances of like-minded business and public officials with the aim of creating a platform for collaboration and capacity building. The goal: mobilization of stakeholders in business and government through the use of policy advocacy,

seminars, workshops and training programmes to create awareness and buy-in of economic and policy actors in creating a sustainable business environment through anti-corruption activities.

The initiative has thus far achieved several accomplishments, including:

- increased dialogue between key actors in the oil and gas industry, one of Nigeria's largest industry sectors, on issues of fraud and corruption;
- raised awareness on the corruption problematic in the country and on the specific issues pertaining to how to eliminate corruption in procurement processes;
- engaged a significant number of SMEs in joint dialogue.⁴¹

The above success stories have shown that multi-stakeholder initiatives, and public-private partnerships are strong anti-financial crime measures. A partnership between Authorities managing Free Trade Zones, Business Enterprises, Financial Institutions and Dedicated Free Zone Customs, Police and Immigration Command assigned to deal with aspects of movement of goods and persons in and out of the Free Zones for information sharing can help identify illicit assets. This partnership should have a legal backing. The proposed law should provide Authorities managing Free Trade Zones, Business Enterprises, Financial Institutions and Dedicated Free Zone Customs, Police and Immigration Command assigned to deal with aspects of movement of goods and persons in and out of the Free Zones with the ability to share information with one another, under a safe harbor provision that offers protections from civil liability, in order to better identify and report potential financial crimes.

4. CONTEXTUAL REVIEWS

Free Trade Zones have proliferated in recent years, such that today there are more than 3,500 free trade zones, often located at key ports, in 130 countries or economies in North and South America, the Asia-Pacific region, Europe and Africa, up from just 79 spread across 25 countries or economies in 1975. (OECD 2019). The special zones facilitate trade by offering businesses advantageous tariffs and lighter regulation on financing, ownership, labour and immigration, and taxes.⁴² The case studies included in the 2010 Financial Action Task Force report illustrate ways in which Free-Trade Zones are misused for money laundering and terrorist financing (Financial Action Task Force, 2010). In particular, the cases highlight the following systemic weaknesses that make Free-Trade Zones vulnerable to abuse:

- Inadequate anti-money laundering (AML) and combating the financing of terrorism (CFT) safeguards;

- Relaxed oversight by competent domestic authorities;
- Weak procedures to inspect goods and register legal entities, including inadequate record-keeping and information technology systems; and
- Lack of adequate coordination and cooperation between zone and Customs authorities.⁴³

Yan Lixin and Tong Wenjun in Money Laundering and Anti-Money Laundering in Free Trade Zones: International Experience and Shanghai Strategies revealed that the Free Trade Zones across the world prove to be extremely attractive to money launderers and terrorist financiers for their loose regulations due to the following reasons: (1) absence or inadequacy of AML and anti-terrorist financing (ATF) framework; (2) loose regulation and low transparency; (3) great difficulty in cross-system/department coordination; and (4) “natural” ML risks brought about by high risk goods.⁴⁴

Anton Moiseienko, Alexandria Reid and Isabella Chase in their paper Improving Governance and Tackling Crime in Free-Trade Zones identified factors that render Free-Trade Zones vulnerable to illicit trade and financial crime and proposes measures to detect and prevent it (Anton Moiseienko, Alexandria Reid and Isabella Chase, 2020). To explore common challenges and responses that transcend countries’ individual circumstances, it examined four country case studies: Morocco, Panama, Singapore and the UAE. Based on 74 interviews, two research workshops and an analysis of publicly available literature, the paper identified key challenges faced by the case study countries, which are also likely to apply to other countries that host Free-Trade Zones:

- The lack of consistent international standards and incentives for the policing of goods that pass through Free-Trade Zones in transit.
 - Inadequate understanding of Free-Trade Zone-related criminal risks in general and financial crime risks specifically, including at the stage of planning and approving the establishment of a Free-Trade Zone.
 - Uncertainty in the division of responsibility for the monitoring, governance and regulation of Free-Trade Zones, including limited information sharing and failure to involve customs agencies in Free-Trade Zone-level risks assessment.
 - The absence of credible monitoring of Free-Trade Zone administrators and users, as well as the resulting gap in enforcement.
 - The lack of proportionate sanctions and AML/CTF supervision of Free-Trade Zone-based businesses that would take account of the risk profile and volume of Free-Trade Zone activities.
 - Limited cooperation with the private sector.⁴⁵
- Although the above-mentioned publications examined a whole range of crimes in Free Trade Zones, they did not provide an explicit explanation for how authorities managing Free Zones can assess the inherent cross-border financial crime risks in Free Trade Zones. This research paper describes the ways in which cross-border financial crime risks can be assessed and adequately addressed by the authorities managing Free Trade Zones. This research paper analyses the risk assessment topic in line with the African Continental Free Trade Area with a focus on Free Trade Zones in Nigeria.

Internationally, this research paper would be the first comprehensive research on the assessment and mitigation of cross-border financial crime risk(s) in Free Trade Zones. This research would

help authorities managing Free Trade Zones, commercial organisations and business enterprises to identify, prevent and mitigate cross-border financial crime risks.

Zone managements and Business enterprises that implement the risk-based approach, in line with the guidance given in this research, will be well-placed to avoid the consequences of inappropriate de-risking behaviour.

5. METHODOLOGY OF THE RESEARCH

The doctrinal legal research methodology would be employed in this study. This methodological strand is described below.

5.1 Doctrinal or Library Based Research Methodology

This research will rely on primary and secondary sources drawn from the public domain.

In order to understand the cross-border financial crime risks associated with the African Continental Free Trade Area and the risk control measures to combat cross-border financial crime in the African Continental Free Trade Area, this research analyzed various documents and reports such as the Agreement Establishing the African Continental Free Trade Area; Nigeria Export Processing Zones Act 1992; Investment Procedures, Regulations and Operational Guidelines For Free Zones In Nigeria, 2004; the Financial Action Task Force 2013 Guidance on National money laundering and Terrorist Financing Risk Assessment; Transparency International 2020 Corruption Perceptions Index; Walk Free Foundation 2018 Global Slavery Index; and United Nations Office on Drugs and Crime 2018 on Drug Use in Nigeria.

6. RESULTS

This section identifies the cross-border financial crime risks that are of priority concern to African Continental Free Trade Areas and shows how countries can assess these risks. The purpose of the analysis is to help the public and private sectors recognize and understand the importance of assessing risk at a zonal level.

6.1 Illicit Finance Activity

Misuse of legal entities to hide a criminal beneficial owner or illicit source of funds is a common feature of money laundering and corruption schemes.⁴⁶ According to the Financial Transparency Coalition, anonymous owners of company and property contribute to the nearly US\$1 trillion illicitly leaving emerging economies. Out of that, an estimated US\$15.7 billion of illicit financial flow is said to pass through the Nigerian financial system annually.⁴⁷

Criminals could misuse front companies, which have legitimate operations in a free trade zone allowing illicit proceeds to be comingled with earnings from legitimate operations. Furthermore, these front companies could be secretly owned by politically exposed persons and high net worth individuals.⁴⁸ Much more challenging for law enforcement are those circumstances where the

shares of front companies are transferred to criminals, which effectively changes the ownership of the companies' assets.⁴⁹

The Authority managing Free Trade Zones should determine the due diligence requirements appropriate to each business enterprise. This may include:

- A standard level of project due diligence, to be applied to all business enterprises.
- An increased level of project due diligence in respect of those business enterprises that are determined to be of higher risk. This may be the result of the company's business activity, ownership structure, anticipated or actual volume or types of business activities, including those activities involving higher risk countries or defined by applicable law or regulation as posing higher risk.
- The standard level being reduced for existing long-term partnerships because the Authority managing Free Trade Zones will have a better knowledge of their partner's operations and policies. However, a new partnership or business relationship may be equally low risk as long as proper due diligence is conducted.

The latest technological innovations that combine Intelligent automation, Artificial Intelligence and machine learning with Know Your Business (KYB)/Know Your Customer (KYC) domain expertise can create a holistic view of business relationship risk through simulation features that grants integrated access to external data sources for customer risk profile enrichment and an Artificial Intelligence-enabled predictive customer risk scores for accurate high-risk customer management.

Ultimate beneficial ownership information is identified using optical character recognition and natural language processing. The implementation of these technologies provides the ability to pull out specific pieces of information or relationships between information from text. Unsupervised machine learning groups documents based on common themes. Relevance scores calculate how well each document belongs to each topic.

The Authority's written policies, procedures, and controls should effectively risk rate business enterprises – either: HIGH, MEDIUM or LOW risk at the project due diligence stage. The Authority's risk rating methodologies should be designed to evaluate business enterprises based on specific company/project information and balanced consideration of all relevant factors, including country/jurisdictional risk, products and services provided, and nature of the company's profiles. The Authority should have up-to-date, accurate, and verified information on business enterprises to enable it to conduct its annual risk assessment.⁵⁰

The Authority managing Free Trade Zones should verify a company's basic information regularly according to the level of risk of the business enterprise. Verification on business enterprises with higher risk level should be carried out at least once per 6 months. Verification on business enterprises with medium risk level should be carried out yearly while verification on business enterprises with low risk should be carried out every two years.⁵¹

6.2. Drug Trafficking

Drug trafficking is a global illicit trade involving the cultivation, manufacture, distribution and sale of substances which are subject to drug prohibition laws.⁵² At current levels, world heroin consumption (340 tons) and seizures represent an annual flow of 430450 tons of heroin into the global heroin market.⁵³

The scale of illicit drugs supply is best estimated by considering demand. The 2018 National Survey on Drug Use and Health had revealed that an estimated 14.4 per cent (range 14 per cent - 14.8 per cent) of the population in Nigeria, or 14.3 million people between 15 and 64 years of age had used drugs, excluding alcohol and tobacco, in 2017. Cannabis was the most widely used substance in the past year in Nigeria, followed by pharmaceutical opioids (mainly tramadol, and to a lesser extent codeine or morphine) and cough syrups containing codeine or dextromethorphan.⁵⁴

The illicit drugs market has diversified in recent years to include the manufacture of skunk and cocaine, which can be bought online or imported by criminal gangs. Recently, it was reported in the Guardian Newspapers that Operatives of the National Drug Law Enforcement Agency (NDLEA) had discovered three major inter-state drug cartels supplying illicit substances to some states in the north. The agency also recovered skunk and cocaine weighing over 843 kilogrammes and arrested no fewer than seven of drug kingpins behind the syndicates in separate raids carried out in Kogi, Nasarawa and Benue states. NDLEA spokesman, Femi Babafemi, in a statement said that the cartels were intercepted on July 12 at a jetty in Idah, Kogi, in a car marked Lagos SMK 345 CG, loaded with 487 kilogrammes of cannabis.⁵⁵

In Nasarawa State, a team of NDLEA operatives had on July 8 raided one of the most hostile drug joints in the state capital. More than 356 kilogrammes of cannabis and various psychotropic substances were recovered. This is addition to the arrest of four major drug dealers, including the most notorious drug kingpin in Nasarawa State. His drug distribution tentacles cut across Kano State, Plateau, Benue and parts of the Federal Capital Territory, Abuja. Curiously, some quantities of cocaine were intercepted in Benue on July 8, July 9t and July 13. Indeed, the supplier was arrested with 29.17 grammes of crack cocaine. In another raid on July 13, the Benue command also seized some quantities of cocaine.⁵⁶

Cannabis, tramadol, and to a lesser extent codeine or morphine could be purchased online, and shipped in large quantities to drug cartels operating as business enterprises in the free trade zones in Nigeria with legitimate products. Drug cartels buying these drugs online or importing the drug or its precursors from other countries in Africa and elsewhere are more likely to use a variety of methods to pay for illegal drugs sold online and acquire additional supply. Some of the methods include bulk cash smuggling, structured cash deposits, funnel accounts, bank wires and virtual currencies and other alternative payment methods, which can often be used anonymously. According to the Drug Enforcement Administration (DEA) and HSI Office of Intelligence, bitcoin and other virtual currencies are used by individuals in the United States to pay for illegal drugs sold online. Virtual currencies are also being used by money launderers in the layering phase to transfer illicit proceeds internationally.

Drug cartels operating as business enterprises in the free trade zones in Nigeria could use all available methods to move and launder illicit proceeds, including bulk cash smuggling, which involves moving currency illicitly into or out of the country; Trade-based money laundering (TBML), which most often involves using illicit proceeds to buy goods for export, as the subsequent sale of the goods effectively launders the proceeds; misuse of financial services providers, by disguising the identity of the customer and/or the nature of the business relationship; virtual currencies and other alternative payment methods, which can often be used anonymously; and transfers via banks and money service businesses (MSBs).

Domestic retail traffickers coordinating cannabis and tramadol sales and distribution outside the free trade zones in Nigeria on behalf of criminal business enterprises are more likely to generate illicit proceeds from street sales. Domestic retail traffickers could launder proceeds using cash, money orders, and structured bank deposits.

The Authority managing Free Trade Zones should begin their risk identification/assessment process with desk-based research into the systems and procedures for importing goods into the Free Zone, and the merchants supplying goods and services to the zone before investigating identified risks to determine the most vulnerable systems, procedures and merchants for drug trafficking. The investigation should be carried out using employee surveys, detailed engagement and discussions with expert stakeholders.⁵⁷ This measure will help to adequately identify the high-risk areas and it will make enhanced due diligence measures more effective.

The Authority managing Free Trade Zones should apply Enhanced Due Diligence measures on a risk-sensitive basis in any situation which by its nature can present a higher risk of drug trafficking. As part of this, the Authority managing Free Trade Zones may conclude, through desk-based research and self-assessments, that certain merchants qualify as possible high-risk merchants. In this situation, the selected merchants must undergo site-based audits. These audits are conducted by independent, third party audit firms. It is acknowledged that participation in the audits can have a material cost implication for host community suppliers and in these cases, the Authority managing Free Trade Zones are advised to subsidise the costs related to the audit.

Audits have a role to play in helping companies assess risk and implement improvement action. Audits provide the additional benefit of engaging merchants in the conversation around ethical trading and drug trafficking (in many cases for the first time). They lead to dialogue on how these challenging issues can be addressed, especially in countries where this may be contrary to historical employment practices.

Financial institutions can play a critical role in combating drug trafficking by implementing a written project due diligence program appropriate for its size and type of business. The program must include risk-based identity verification, recordkeeping, and retention procedures, as well as procedures to determine whether the financial system could be used by drug cartels to pay for illegal drugs sold online and to move and launder illicit proceeds and to take appropriate follow-up action if a business enterprise is designated as high risk. Project due diligence helps a company determine the risks posed by a particular merchant, allowing the institution to ensure

that it has the proper controls in place, including suspicious activity monitoring procedures, and to monitor and report on the risks of a particular merchant.

6.3. Trade Based Money Laundering

The Financial Action Task Force defines trade-based money laundering (TBML) as the process of disguising the proceeds of crime and moving value through the use of trade transactions in an attempt to legitimize their illicit origin (Financial Action Task Force, 2006).⁵⁸ TBML refers to a variety of schemes that can involve moving illicit merchandise, falsifying the value of merchandise, and misrepresenting trade-related financial transactions with the purpose of disguising the origin of criminal proceeds and integrating the funds into the financial system.⁵⁹

Transnational criminal organizations could exploit the import and export system of the African Continental Free Trade Area to disguise, convert and transfer criminal proceeds through movement of goods as well as funds.⁶⁰ This can occur through the sale of underpriced imported goods purchased with illicit proceeds. The aim is to expedite the money laundering process. The below market pricing is a cost of doing business for the money launderer, but it puts legitimate businesses at a competitive disadvantage. This activity can create a barrier to the African Continental Free Trade Agreement, crowding out legitimate economic activity. TBML also robs governments of tax revenue due to the sale of underpriced goods, and reduced duties collected on undervalued imports and fraudulent cargo manifests.

TBML could involve criminals conspiring with dealers in precious metals and stones for the laundering of tainted money. In this money laundering scheme, the dealer in precious metals and stones who is operating in one of the free trade zones in Nigeria will accept the tainted cash, from the criminals, and in exchange would send the corresponding value, minus a commission, via wire transfers to the destination country in a manner designed to conceal and obfuscate the source or owner of the tainted funds. The dealer in precious metals and stone will deposit the tainted cash in the business's bank account as if it had been received over the counter from retail customers, and maintain false invoices in its records to justify the wires as payments for gold although no gold was received. Criminals could also undervalue legitimate gold shipments from Nigeria to evade the tax due. This tax evasion scheme can be detected by law enforcement agents by comparing the declared value of the gold with its actual market value.

In a separate scheme, the dealer in precious metals and stones could overvalue legitimate gold shipments from Nigeria for TBML. This happens when an amount larger than the purchase price is paid to the dealer in precious metals and stones and an arrangement is made to have the balance paid as directed into different bank accounts of 'money mules'. The funds would later be transferred back into the criminal's main account after deducting their commission. This can legitimise large amounts of illicit funds. Merchants may also be unwitting participants in this money laundering scheme where a complaint of refund is made by a buyer who claimed to have paid way more than the purchase price. The buyer will ask the merchant to transfer the balance paid to a different bank account.

Another form of TBML to which banks in the free trade zones are exposed is through the abuse of the open account third party payments system. This is the process by which sellers extend credit to purchasers and ship goods in advance of payment. Third parties can then make payments to the seller to settle the open account debts, providing a risk of these debts being settled using illicit funds. In addition, banks can be exposed to money-laundering through documentary trade finance, whereby fraudulent documents are used to launder funds through the trade system.

The Authority managing Free Trade Zones must develop risk-based policies, procedures, and controls that are reasonably designed to (a) gather all relevant due diligence information concerning trade in goods and trade in services, (b) verify the due diligence information by reviewing certified copies of Commercial Invoices, Packing List, Bill of Lading and other relevant documents, (c) employ this due diligence information to determine whether a Free Zone Enterprise is subject to enhanced due diligence, (d) conduct assessments of money laundering risks for each merchant, including a periodic review of the trade activity to determine consistency with information obtained about the type, purpose, and anticipated activity of the merchant, (e) appoint one or more competent persons as inspectors to investigate the affairs of any Free Zone Enterprise and report to the Authority in such form and within such time as it may direct. Such appointment may be made on the application of the Owner, or of the Free Zone Enterprise or by any creditor of the Owner or of the Free Zone Enterprise or by the Authority acting unilaterally or by any other person provided the Authority is satisfied that good reason has been shown or circumstances arisen for requiring the investigation.⁶¹ If the Free Zone Registrar has reasonable cause to believe that any Free Zone Enterprise is not carrying on business in line with the anticipated activity, it may deregister the Free Zone Enterprise after enquiry in writing of the Free Zone Enterprise to ascertain if it is carrying on legitimate business and such Free Zone Enterprise either failing to respond to such enquiry within 7 days thereof or failing to demonstrate to the satisfaction of the Authority that it is carrying on business in line with the approved activity.⁶² The Free Zone Registrar should also file a suspicious activity report with the financial intelligence unit as it concerns the illegal activity of the Free Zone Enterprise.⁶³

Financial institutions should develop sufficient policies and procedures to assess the trade based money laundering risks associated with providing financial services to business enterprises in free trade zones.⁶⁴ The bank's customer identification program should detail the identification requirements for opening an account for a Free Zone Enterprise.⁶⁵ When opening an account for a customer that is not an individual, banks should obtain information about the individuals who have authority and control over such accounts in order to verify the customer's identity (the customer being the business entity).⁶⁶ Required account opening information may include articles of incorporation, a corporate resolution by the directors authorizing the opening of the account, or the appointment of a person to act as a signatory for the entity on the account. Particular attention should be paid to articles of association that allow for nominee shareholders, board members, and bearer shares.

The latest technological innovations that combine Intelligent automation, Artificial Intelligence and machine learning with Know Your Customer (KYC)/Customer Due Diligence (CDD) domain expertise can create a holistic view of customer risk through simulation features that

grants integrated access to external data sources for customer risk profile enrichment and an Artificial Intelligence-enabled predictive customer risk scores for accurate high-risk customer management.

Ultimate beneficial ownership information is identified using optical character recognition and natural language processing. The implementation of these technologies provides the ability to pull out shareholder information contained in official company documents purchased from government registers. Unsupervised machine learning groups documents based on common themes. Relevance scores calculate how well each document belongs to each topic.

Risk assessments may include a review of the domestic or international jurisdiction where the Free Zone Enterprise was established, the type of account (or accounts) and expected versus actual transaction activities, the types of products used, and whether the business entity was created in-house or externally.⁶⁷

7. THE WAY FORWARD

The Authority managing Free Trade Zones should integrate the findings from their risk assessments across relevant internal functions and processes, and take appropriate action. This will enable them to prevent and mitigate adverse financial crime risks.

Effective mitigation requires that:

- (i) Responsibility for addressing such risks is assigned to the appropriate level and function within the business enterprise;
- (ii) Internal decision-making, budget allocations and oversight processes enable effective responses to such risks.

Appropriate action will vary according to:

- (i) Whether the business enterprise causes or contributes to an adverse financial crime risks, or whether it is involved solely because the financial crime risks are directly linked to its operations, products or services by a business relationship;
- (ii) The extent of its leverage in addressing the adverse financial crime risks.

Potential financial crime risks should be prevented or mitigated through the horizontal integration of findings across the free trade zones, while actual risks—those that have already occurred – should be a subject for remediation.⁶⁸

The more complex the situation and its implications for the business relationship, the stronger is the case for the Authority managing Free Trade Zones to draw on independent expert advice in deciding how to respond.

If the Authority managing Free Trade Zones has leverage to prevent or mitigate the identified financial crime risks, it should exercise it. And if it lacks leverage there may be ways for the Authority managing Free Trade Zones to increase it. Leverage may be increased by, for example, offering capacity-building or other incentives to the related entity, or collaborating with other actors.

There are situations in which the Authority managing Free Trade Zones lacks the leverage to prevent or mitigate adverse financial crime risks and is unable to increase its leverage. Here, the Authority managing Free Trade Zones should consider ending the business relationship, taking into account credible assessments of potential adverse financial exclusion impacts of doing so.

Where the relationship is “crucial” to the Authority managing Free Trade Zones, ending it raises further challenges. A relationship could be deemed as crucial if it provides a product or service that is essential to the country, and for which no reasonable alternative source exists. Here the severity of the adverse financial crime impact must also be considered: the more severe the financial crime risks, the more quickly the Authority managing Free Trade Zones will need to see change before it takes a decision on whether it should end the business relationship. In any case, for as long as the infraction continues and the Authority managing Free Trade Zones remains in the business relationship, it should be able to demonstrate its own ongoing efforts to mitigate the financial crime risks and be prepared to accept any consequences – reputational, financial or legal – of the continuing connection.

7.1 Mitigating the Illicit Finance Risks Associated with Anonymous Companies

To effectively mitigate the illicit finance risks associated with anonymous companies, every person with significant control over a company should, within seven days of becoming such a person, indicate to the company in writing the particulars of such control.⁶⁹ A company after receiving or coming into possession of such information required, should, not later than one month from the receipt of the information or any change therein, notify the Authority managing Free Trade Zones of that information provided that a company shall in every annual return, disclose the information required in respect of the year for which the return is made.⁷⁰ This measure is in line with Section 119 of the Nigerian Companies and Allied Matters Act, 2020. Section 868(1) of the Nigeria Companies and Allied Matters Act, 2020 defines a “person with significant control” as any person—

- a. directly or indirectly holding at least 5% of the shares or interest in a company or limited liability partnership;
- b. directly or indirectly holding at least 5% of the voting rights in a company or limited liability partnership;
- c. directly or indirectly holding the right to appoint or remove a majority of the directors or partners in a company or limited liability partnership;

d. otherwise having the right to exercise or actually exercising significant influence or control over a company or limited liability partnership; or

e. having the right to exercise, or actually exercising significant influence or control over the activities of a trust or firm whether or not it is a legal entity, but would itself satisfy any of the first four conditions if it were an individual;

The Authority managing Free Trade Zones should maintain a register of persons with significant control in which it shall enter the information received from the company or any change therein.⁷¹ A company should inscribe against the name of every member in the register of members the information received in pursuance of the requirements of this section.⁷² If default is made by any person or company in complying with the above requirements, the person or company and every officer of the company should be liable to such fines as the Authority managing Free Trade Zones may prescribe by regulation for every day during which the default continues.⁷³ Notwithstanding the above provisions, a person who is a substantial shareholder in a company should be required by the Authority managing Free Trade Zones to give notice in writing to the company stating his name, address and full particulars of the shares held by him or his nominee (naming the nominee) by virtue of which he is a substantial shareholder. This measure is in line with Section 120 of the Nigerian Companies and Allied Matters Act, 2020.⁷⁴ A person is a substantial shareholder in a public company if he holds himself or by his nominee, shares in the company which entitle him to exercise at least 5% of the unrestricted voting rights at any general meeting of the company.⁷⁵ A person required to give a notice, shall do so within 14 days after that person becomes aware that he is a substantial shareholder.⁷⁶ The notice shall be given notwithstanding that the person has ceased to be a substantial shareholder before the expiration of the period referred to above.⁷⁷ The company shall, within 14 days of receipt of the notice or of becoming aware that a person is a substantial shareholder give notice in writing to the Authority of this fact.⁷⁸ If any person or company fails to comply with the provisions of this section, the person or the company should be liable to such fines as the Authority may prescribe by regulation for each day the default continues.⁷⁹

Every Free Zone Enterprise shall keep at its Free Zone registered address a register of directors and secretary and the register shall contain details as to the identity and address of the directors and secretary of the Free Zone Enterprise, and of any changes thereto. Any such changes shall be notified to the Free Zone Registry within 14 days thereof and details promptly entered in the Free Zone Enterprise Register in the prescribed form.⁸⁰

In order to ensure the effective implementation of disclosure and transparency measures, the Authority managing Free Trade Zones should increase their focus on professional middlemen e.g. lawyers, notaries and other independent legal professionals who help clients establish legal entities, open bank accounts, and engage in other “transactional” activities. Lawyers, notaries and other independent legal professionals should be required to implement customer due diligence and record-keeping requirements set out in Recommendations 10, 11, 12, 15, and 17 of the Financial Action Task Force Recommendations when they prepare for or carry out

transactions for their client concerning the creation, operation or management of legal persons or arrangements, and buying and selling of business entities. This is in line with Recommendation 22 of the Financial Action Task Force Recommendations 2012 - 2021.⁸¹ Lawyers, notaries, other independent legal professionals and accountants should also be required to implement group-wide programmes against money laundering and terrorist financing, including policies and procedures for sharing information within the group for anti-money laundering and combating the financing of terrorism (AML/CFT) purposes; implement enhanced due diligence measures to business relationships and transactions with natural and legal persons, and financial institutions, from countries for which this is called for by the Financial Action Task Force; report suspicious transactions when, on behalf of or for a client, they engage in transactions concerning the creation, operation or management of legal persons or arrangements, and buying and selling of business entities without disclosing (“tipping-off”) the fact that a suspicious transaction report (STR) or related information is being filed with the financial intelligence unit (FIU). These measures are in line with Recommendation 23 of the Financial Action Task Force Recommendations 2012 - 2021.⁸²

7.2 Mitigating the Drug Trafficking Risks Associated with the Exploitation of the Import and Export System of the African Continental Free Trade Area

Monitoring the effectiveness of a company’s actions to identify and prevent drug trafficking could be a challenge across the Free Trade Zones. One way that the Authority managing Free Trade Zones can monitor activities at manufacturing site level is through unannounced site visits. Business enterprises should be required to have a whistle-blowing policy which shall be made known to employees, management, directors and other stakeholders such as contractors, shareholders, job applicants and the general public.⁸³ The policy should be disclosed in their web sites. It is the responsibility of the board to implement such a policy and to establish a whistle-blowing mechanism for reporting any illegal or unethical behavior. Businesses should establish whistleblowing procedures that encourage stakeholders by assurance of confidentiality, to report any unethical activity using, among others, a dedicated email or hotline to the company and the National Drug Law Enforcement Agency. Employees, sub-contractors or suppliers who become aware of possible improper, unethical or even illegal behaviour should be allowed to raise the matter with their manager or alternatively refer the matter to a confidential and independent telephone number.

In order to further mitigate the money laundering risks associated with the exploitation of the import and export system of the African Continental Free Trade Area, every Free Zone Enterprise should be required to keep accounting records sufficient to show and explain the transactions of such Free Zone Enterprise.⁸⁴ Ongoing account monitoring is critical to ensure that bank accounts are reviewed for trade based money laundering activities.⁸⁵ Banks in Free Trade Zones should be aware of higher-risk transactions in these accounts, such as activity that has no business or apparent lawful purpose, funds transfer activity to and from higher-risk jurisdictions, currency intensive transactions, and frequent changes in the ownership or control of the nonpublic business entity.⁸⁶ The type of monitoring framework implemented will depend on a financial institution’s risk assessment and so will vary between institutions and even between

business units within a financial services group. Based on this risk assessment, the development of an appropriate monitoring framework will depend both on the products and services being supported, the size and nature of the institution's operations and, where appropriate, the adoption of a risk-based approach. The results of this assessment will determine whether an institution opts for a single approach to monitoring or deploys a combination of monitoring activities.⁸⁷ Banks must ensure that their automated monitoring system captures not only the amount and date of a transaction but also the identity or geographic location of the persons sending or receiving the wires. Failure to do this may lead to a situation where the Bank is unable to identify and investigate potentially suspicious transactions based on the presence of important risk factors, such as jurisdiction and the potential involvement of politically-exposed persons (PEPs).

Using a sophisticated, end-to-end anti-money laundering solution, that combines out-of-the-box rules-based models with intelligent segmentation and automated simulation and profiling analytics to detect known risks with advanced analytic techniques – including machine learning and deep learning – to identify unknown risks and hidden relationships will help to ensure accurate alert detection, increased team productivity and lowered compliance program costs. As a result, antimoney laundering departments can more effectively monitor suspicious activities.

7.3 Mitigating the Trade Based Money Laundering Risks Associated with the Exploitation of the Import and Export System of the African Continental Free Trade Area

Countries should assess the risk of trade based money laundering in their free trade areas. The first stage of the assessment, identification, should focus on gathering information through desk-based research and self-assessment questionnaires.⁸⁸ The deskbased research should review the procedures for Importing Goods Into The Free Zone, the Cargotrack Inventory System, procedures for Exporting Goods From The Free Zone Into The Customs Territory, Procedures For Goods Being Transferred From One Licensee To Another Within A Zone, Procedures For Transferring Goods Between One Free Zone And Another, Free Zone Registry Procedures And Regulations, Taxation Procedures And Regulations, Banking Procedures & Regulations, the Dedicated Free Zone Customs, Police and Immigration Command assigned to deal with aspects of movement of goods and persons in and out of the Free Zones, the number of public officials involved in the licensing and registration of free zone enterprises, previous financial crime reports by government and non-governmental organizations and whistleblowing reports.

Countries can also gather intelligence surrounding new and emerging risks through their domestic team of financial crime specialists, Custom Agencies, Law Enforcement Agencies, Financial Intelligence Units, Tax Authorities, Banking Supervisors, Supervisory Authorities, other government departments and non-governmental organisations (NGOs). Journalists and activists can also play an important role in helping countries identify exactly where some of the biggest financial crime risks may lie. We recognize the important role that investigative journalism can play in identifying current and emerging risks. This approach will help countries to identify where the most salient and material risks exist within their free trade areas. From there, the country involved will collaborate with them and work closely to learn from their experiences wherever possible.

Countries should engage with those free trade zones that have been identified as potentially high risk and work with them to complete a range of assessment questions to better understand what controls they have in place and to develop risk mitigation plans for any identified issues. The self-assessment questionnaire should be structured around the key areas of the zone's Code of

Conduct for preventing financial crime and provide the country with information on the policies, procedures and practices the free trade zone has in place to effectively manage these risks.

The free zone enterprise self-assessment questionnaires should be updated regularly to align closely with requirements set out in the voluntary Code of Conduct for Clean Free Trade Zones that is set out in the Appendix to the OECD, Recommendation of the Council on Countering Illicit Trade: Enhancing Transparency in Free Trade Zones.⁸⁹ The self-assessment questionnaires should be designed to gauge compliance with the standard, identify potential financial crime risks and flag where further intervention is required, including the possibility of site-based audits.

Countries can use the RUSI Free Trade Zone Risk Assessment tool to assess their exposure to the risk of facilitating illicit trade or financial crime in any Free Trade Zone.⁹⁰ The tool which comes with a self-assessment questionnaire helps assess the user's exposure to the risk of facilitating criminal conduct. It does so by:

- Facilitating a well-informed view of a Free Trade Zone's criminal vulnerabilities and mitigation measures. The tool guides the user through assessing the factors that determine a Free Trade Zone's criminal risk profile. It identifies 11 such factors common to Free Trade Zones, provides a framework for their assessment and lists sources of relevant information. The tool is designed to produce a numerical Free Trade Zone risk score, but it can also be used by compliance and investigation professionals as a first step in analysing how a particular Free Trade Zone can be used for crime.
- Identifying a Free Trade Zone's overall risk level. The assessment of Free Trade Zone risk factors will result in an overall risk score that can be used by compliance professionals as a supplement or alternative to country risk scores. This will result in more accurate risk assessment for Free Trade Zone-related transactions because a Free Trade Zone's risk profile may differ from that of the country where it is located.⁹¹

Where the results of the self-assessment highlights minor areas for improvement, the constituted authority should work with the free zone enterprise to develop corrective actions and agree on a timescale for material progress towards compliance.

Where the results reveal more significant issues, enhanced due diligence measures should be adopted.

Countries must apply Enhanced Due Diligence measures on a risk-sensitive basis in any situation which by its nature can present a higher risk of financial crime. As part of this, a country may

conclude, through desk-based research and self-assessments, that certain free trade zones qualify as possible high-risk zones. In this situation, the selected zone must undergo site-based audits.

These audits should be conducted by independent, third-party audit firms. Countries should consider integrating 'experience-based sample surveys' into part of their on-site audits programme as a means of ensuring that the data is accurate. Experience-based surveys can avoid the pitfalls of both administrative data on illicit trade and financial crime (namely the pervasive undercounting of undetected and unreported cases) and the shortcomings of perception-based corruption studies (which by definition capture opinions rather than the actual phenomenon). When well designed and implemented to the highest standards, experience-based surveys on illicit trade and financial crime can measure both levels of and trends in illicit trade and financial crime.

Audits have a role to play in helping companies assess risk and implement improvement action. Audits provide the additional benefit of engaging shareholders, directors and the management team of business enterprises in the conversation around ethical trading and financial crime. They lead to dialogue on how these challenging issues can be addressed, especially in countries where this may be contrary to historical employment practices.

Countries should work with the relevant stakeholders, prepare a draft programme and coordinate the logistics for free zones that need on-site audit. The draft programme, together with any specific logistical arrangements, should be forwarded to the independent auditor no later than 3 weeks before the visit. The draft programme should take into account the areas where the assessment team may want to apply increased focus.

The on-site visit provides the best opportunity to clarify issues relating to the business enterprises' system, and independent auditors need to be fully prepared to review the Outcomes relating to the effectiveness of the system, and clarify any outstanding technical compliance issues. Independent auditors should also pay more attention to areas where illicit trade and financial crime risks are identified. Independent auditors must be cognisant of different countries' circumstances and risks and they should understand that countries may adopt different approaches to create an effective system and meet the global Standards for clean free trade zones. Independent auditors should therefore be open and flexible, and seek to avoid narrow comparisons with their own national requirements.

Countries could use the World Free Zones Organization (World FZO) Safe Zone Certification Program for site-based audits in order to properly assess whether a free zone has implemented best practices to promote clean trade within its borders.⁹² The Safe Zone Certification Program is designed in line with the WCO's SAFE Framework and strictly adhering to the OECD's Code of Conduct, to enable such serious free zones to demonstrate their compliant business practices with a new global compliance standard. A key aspect of this program is the internationally recognized third-party vetting that the independent site inspection provides.

As a free zone voluntarily submits to inspection, it enhances its transparency and commitment to clean trade, promoting itself as a compliance champion on the global trade landscape.

The program has two main stages – first, an application and independent online assessment, then a site inspection of Safe Zone qualifying elements by internationally recognized third-party validators. The result of this process leads to either Prospect status, where free zones fall short of the certification criteria but are given a roadmap to correct any deficiencies over a 12 month period before re-inspection; or Platinum status, where free zones are confirmed as Safe Zone compliant.⁹³

Where issues have been identified in certain free trade zones through investigations that were carried out at the Enhanced Due Diligence stage, countries must determine how such issues can best be remediated or mitigated through measures such as training and awareness, whistle-blowing mechanisms, and industry collaboration or improved purchasing practices internally.

In order to further mitigate the money laundering risks associated with the exploitation of the import and export system of the African Continental Free Trade Area, law enforcement agents should increase their focus on complicit merchants who are facilitating trade-based money laundering (TBML), as well as Professionals, including individuals in the financial sector, accountants, real estate agents, and lawyers. Individuals who abuse their professional position at financial institutions also are a money laundering risk. These individuals facilitate the opening of accounts, conduct funds transfers, and cash checks while knowingly failing to verify customer identification when required, maintain accurate transaction records, or file required reports. Financial institutions with lax compliance programs also pose a money laundering risk. Finally, pursuing global money laundering syndicates requires law enforcement to partner with other countries to help trace illicit proceeds, identify relevant parties, collect evidence, and seize assets.

8. CONCLUDING REMARKS

This paper identified illicit finance activity, drug trafficking and trade-based money laundering as financial crimes typologies of priority concern to African Continental Free Trade Areas and demonstrated how countries can assess and mitigate these risks through adequate policies, procedures, and controls including appropriate compliance management arrangement and adequate screening procedures to ensure high standards when hiring employees; corporate transparency; training on managing incidents of drug trafficking; and appropriate monitoring framework for illicit finance activities and trade based money laundering activities.

The purpose of the analysis is to help the public and private sectors recognize and understand the importance of assessing and mitigating financial crime risks at a zonal level.

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